

RESPONSE OF THE OFFICE OF  
PUBLIC UTILITY REGULATION

Our Ref. No. 03-8-OPUR  
Evercore METC Investment Inc.,  
Et Al.

DIVISION OF INVESTMENT MANAGEMENT

File No. 132-3

Based on the facts and representations in your letter of November 25, 2003, and without necessarily agreeing with your legal analysis, we would not recommend any enforcement action to the Commission under sections 2(a)(7) and 2(a)(11)(A) of the Public Utility Holding Company Act of 1935 against Evercore METC Investment Inc., Evercore METC Coinvestment Inc., Macquarie Transmission Michigan Inc., NA Capital Holdings Inc., and Michigan 1400 Corp. (collectively, the "Limited Partners") solely because the Limited Partners participate in the proposed Transaction under the circumstances described in your letter.

You should note that facts or conditions different from those presented in your letter might require a different conclusion. Further, this response expresses only the Division's position on enforcement action. It does not purport to express any legal conclusion on the questions presented.



David G. LaRoche  
Special Counsel

November 25, 2003



OFFICE OF  
PUBLIC UTILITY REGULATION

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

November 25, 2003

William S. Lamb, Esquire  
LeBoeuf, Lamb, Greene & MacRae L.L.P.  
125 West 55th Street  
New York, NY 10019-5389

Re: Evercore METC Investment Inc., et al.  
File No. 132-3

Dear Mr. Lamb:

Enclosed is our response to your letter of November 25, 2003. By incorporating our answer in the enclosed copy of your letter, we avoid having to recite or summarize the facts involved.

Very truly yours,

A handwritten signature in cursive script that reads "David G. LaRoche".

David G. LaRoche  
Special Counsel

Enclosure

LEBOEUF, LAMB, GREENE & MACRAE  
L.L.P.

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November 25, 2003

Ms. Catherine A. Fisher  
Assistant Director  
Securities and Exchange Commission  
Division of Investment Management  
Office of Public Utility Regulation  
450 Fifth Street N.W.  
Judiciary Plaza  
Washington, D.C. 20549

Re: Evercore METC Investment Inc., et al.  
Public Utility Holding Company Act of 1935  
Sections 2(a)(7) and 2(a)(11)

Dear Ms. Fisher:

We are writing on behalf of Evercore METC Investment Inc. ("EMI"), Evercore METC Coinvestment Inc. ("EMC"), Macquarie Transmission Michigan Inc. ("MTM"), NA Capital Holdings Inc. ("NA Holdings"), and Mich 1400 Corp. ("Mich 1400"), (collectively, the "Limited Partners") in connection with a proposal, as described below, to acquire an 85% limited partnership interest (the "Limited Partnership Interest") in Michigan Transco Holdings, Limited Partnership (the "Partnership"), a Michigan limited partnership that owns 100% of the limited liability company interests of Michigan Electric Transmission Company LLC, a Michigan limited liability company ("Transco"). Transco owns electric transmission facilities and related assets located in the state of Michigan. The acquisition of the Limited Partnership Interest by General Electric Capital Corporation ("GE Capital") was previously addressed in a no-action letter from the Division of Investment Management (the "Staff") to GE Capital, dated April 26,

2002 (the "GE Letter"). The Limited Partners are purchasing the Limited Partnership Interest from SFG V-A, INC., an indirectly wholly owned subsidiary of GE Capital.

This letter requests your written confirmation that, as a result of the proposed transaction described below, the Staff will not recommend that the Securities and Exchange Commission (the "Commission") institute enforcement action under the Public Utility Holding Company Act of 1935, as amended (the "Act") to deem the Limited Partners to be "holding companies" or "affiliates" (as such terms are defined in Sections 2(a)(7) and 2(a)(11)(A) of the Act, respectively) of the Partnership, Transco or any of their subsidiaries.

## **I. Factual Background**

### **A. Description of the Parties<sup>1</sup>**

The Partnership. The Partnership is a single-purpose Michigan limited partnership<sup>2</sup> formed by Trans-Elect, Inc. ("Trans-Elect"), a Michigan corporation, for the purpose of holding Transco.<sup>3</sup> The sole general partner of the Partnership is Trans-Elect Michigan, LLC ("TE Michigan"), a single-purpose, single-member Michigan limited liability company that is wholly-owned by Trans-Elect (Trans-Elect and TE Michigan are collectively referred to herein as the "General Partner"). The sole limited partner of the Partnership is SFG V-A INC. ("SFG"), a Delaware corporation which is wholly-owned by GE Capital Services Structured Finance Group, Inc. ("GE Capital SFG"), a Delaware corporation. GE Capital SFG is wholly-owned by GE Capital.

Transco. Transco owns an electric transmission system and related assets located in Michigan. These assets include approximately 5,400 miles of 345-kilovolt and 138-kilovolt transmission lines and associated substations and other facilities serving the service territory of Consumers Energy Company, an unaffiliated public utility company. Transco is an "electric

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<sup>1</sup> An organizational chart depicting the ownership structure among the parties that would be in place immediately following the proposed transaction is included as Attachment 1 hereto.

<sup>2</sup> The Partnership may be converted into a limited liability company in the future. The Limited Partners expect that as long as the consent rights of any non-managing members of a limited liability company are less extensive or equivalent to the consent rights held by the Limited Partners, they could continue to rely on the Staff's response to this no-action request.

<sup>3</sup> In a transaction described in more detail in the GE Letter, Consumers Energy Company formed a wholly owned subsidiary, Michigan Electric Transmission Company ("METC Corp.") to own its transmission facilities. METC Corp. was then merged with and into Transco.

utility company" as defined in Section 2(a)(3) of the Act. Trans-Elect is the manager of Transco pursuant to a management services agreement (the "Management Agreement").

The General Partner. Trans-Elect, through TE Michigan, is and will continue to be the General Partner of the Partnership. Trans-Elect's focus is the ownership and management of electric transmission systems; it is not a market participant in either electric generation or distribution and is not engaged in power trading or marketing.<sup>4</sup> As described in the GE Letter, Trans-Elect's officers and founders are former utility executives with more than 125 years of combined electric utility industry experience.

Trans-Elect is a privately held company owned by its officers and founders, as well as by various other investors. GE Capital indirectly owns preferred stock (the "Series C Preferred Stock") in Trans-Elect representing approximately 12.5% of Trans-Elect's total equity on an undiluted basis.<sup>5</sup> As part of the proposed transaction, the Limited Partners will acquire the Series C Preferred Stock from GPSF-F INC. ("GPS"), an indirect wholly-owned subsidiary of GE Capital.<sup>6</sup> The remaining investors in Trans-Elect include former utility industry executives, other individuals, venture capital funds and industrial manufacturing companies, none of which is affiliated with the Limited Partners. Although the shareholders of Trans-Elect are parties to a voting agreement with respect to the election of directors, which allows GPS to appoint a director to Trans-Elect's Board of Directors, GPS has waived such right, and the Limited Partners will continue to waive such right in exchange for the right to designate up to two non-voting observers to such Board.

The Limited Partners. EMI has been formed by Evercore Capital Partners II L.P. ("ECP"), and EMC has been formed by Evercore Co-Investment Partnership II L.P. ("ECIP"), an affiliate of ECP. ECP and ECIP are New York and Los Angeles based private equity funds that

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<sup>4</sup> On April 29, 2002, Trans-Elect acquired a 50% general partnership interest in a Canadian consortium (named AltaLink, L.P.) that owns approximately 7,200 miles of high-voltage, high-capacity transmission lines and nearly 260 substations in Alberta, Canada. AltaLink, L.P. is a foreign utility company under Section 33 of the Act. See Notification of Foreign Utility Company Status, filed on Form U-57/A by Trans-Elect on September 9, 2002. Trans-Elect is also a managing member of an entity that is participating in the Path 15 Transmission project in California, which is constructing new transmission capacity in that state.

<sup>5</sup> The fully diluted percentage would be approximately 8.3% after taking into account options and similar securities held by other parties.

<sup>6</sup> As noted below, the Limited Partners will acquire the same proportion of the Series C Preferred Stock as they acquire in the Limited Partnership Interest.

invest in a variety of businesses across a wide range of industries. Their investors include corporate pension funds, endowments, insurance companies, investment trusts, banks and families.

MTM is a wholly owned subsidiary of MEAP US Holdings Ltd., which is itself a subsidiary of Macquarie Essential Assets Partnership ("MEAP"). MEAP is a Canadian limited partnership investing in essential infrastructure assets in Canada and the United States. Its investors currently comprise Canadian pension plans and other institutional investors, as well as an indirect subsidiary of Macquarie Bank Limited. Currently, MEAP's only investment is a 15% indirect interest in AltaLink, L.P. ("AltaLink") which is an independent electricity transmission network owner in Alberta, Canada.<sup>7</sup>

NA Holdings has been formed by the Macquarie group. The parent company of the Macquarie group is Macquarie Bank Limited, an investment bank headquartered in Australia, which is a leading provider of investment, financial markets and advisory products and services. The Macquarie group manages several investment funds that specialize in infrastructure assets in the transportation, water, telecommunications and energy sectors. NA Holdings is a wholly owned subsidiary of Macquarie Holdings Inc. (USA) ("Macquarie Holdings USA"), a New York based affiliate of the Macquarie group. Macquarie group has focused much of its activity in the U.S. on infrastructure investments. Macquarie Holdings (USA) intends to either sell NA Holdings to an un-affiliated investor or transfer NA Holdings to a fund managed by the Macquarie group, either prior to or shortly following the consummation of the Transaction.

Mich 1400 is a wholly-owned subsidiary of Michigan 1400 LLC. Over 97% of the capital committed to Michigan 1400 LLC is from KBRWJ Investors LP ("KBRWJ LP"), a private investment vehicle funded by individuals, trusts and families. KBRWJ LP is also a 27% passive investor in the Path 15 Transmission project in California.

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<sup>7</sup> MTM intends to transfer its shares of Series C Preferred Stock to MEAP US Holdings 2 Ltd immediately following consummation of the Transaction. MEAP US Holdings 2 Ltd is a wholly owned subsidiary of MEAP.

## **B. Description of the Proposed Transaction**

### **1. General**

The proposed transaction (the "Transaction") will consist of the acquisition by the Limited Partners of the Limited Partnership Interest held by SFG and the Series C Preferred Stock held by GPS. The structure described in the GE Letter will not be changed by the Transaction, only the owners of the Limited Partnership Interest and the Series C Preferred Stock will be changed from GE Capital to the Limited Partners, with the corresponding substitution of the Limited Partners for GE Capital's acquisition vehicles, *i.e.*, GPS and SFG.

Although the partnership agreement of the Partnership (the "Partnership Agreement") will be amended in connection with the Transaction, as described below, the day-to-day operations of Transco and the General Partner will not change as a consequence of the proposed transaction. Trans-Elect, the manager of Transco has extensive utility industry management experience and will continue to have the responsibility of controlling and managing the operations of Transco just as it does today. Pursuant to the Management Agreement, Trans-Elect has the same management responsibilities for Transco as the General Partner does for the Partnership under the Partnership Agreement. This control relationship will not change as a result of the proposed transaction. Transco will continue to be a public utility subject to the jurisdiction of the Federal Energy Regulatory Commission ("FERC") under the Federal Power Act, as amended (the "Federal Power Act"). The Michigan Public Service Commission ("Michigan Commission") also will continue to have the authority to regulate certain aspects of Transco's operations, including the siting of new transmission facilities and compliance with health and safety-related rules and regulations.<sup>8</sup> The proposed transaction also will not affect the operational control over Transco's jurisdictional transmission facilities exercised by the Midwest Independent Transmission System Operator, Inc. ("MISO").<sup>9</sup>

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<sup>8</sup> The Partnership will commit to fulfill Transco's obligations under Michigan's Customer Choice and Electricity Reliability Act to expand transmission capability within Michigan pursuant to plans approved by the Michigan Commission.

<sup>9</sup> MISO is an independent, FERC-approved regional transmission organization ("RTO"), which began the functional operation of the transmission assets of various electric utility companies under a single tariff as of February 1, 2002. On April 12, 2002, FERC authorized the transfer of operational control of Transco's transmission assets to MISO. Under the FERC-approved agreement between MISO and the participating transmission owners, including Transco,

The only regulatory or other governmental approval required in connection with the acquisition of the Limited Partnership Interest and the Series C Preferred Stock by the Limited Partners is the approval by the FERC under Section 203 the Federal Power Act.

## 2. Financing Structure

In connection with the closing of the Transaction, it is contemplated that the outstanding debt of the Partnership and Transco will be refinanced with new third party lenders. With the exception of this refinancing, the Transaction will have no effect on the general financial structure of Trans-Elect, the Partnership or Transco, as described in the GE Letter. GE Capital is selling its outstanding Limited Partnership Interest and its outstanding Trans-Elect Series C Preferred Stock to the Limited Partners.

## 3. Structure of the Partnership

The Partnership structure also remains fundamentally unchanged from the structure described in the GE Letter. The Partnership will continue to be a Michigan limited partnership managed by the General Partner in which the Limited Partners will have a passive investment. The Partnership will continue to be operated and controlled by the General Partner, which is in turn controlled by the officers and founders of Trans-Elect, each of whom has significant experience in the electric utility industry. The Limited Partners will maintain a significant economic interest in the Partnership's profits and losses, but will have no control over the day-to-day operations of the Partnership or its operating utility subsidiary, Transco.

Some provisions of the existing Partnership Agreement will, however, be changed as a result of the proposed transaction in order to make the Partnership a more attractive investment vehicle for financial investors. In general, the amendments would:

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MISO will be responsible for scheduling all transmission service, except that MISO may grant transmission owners the authority to schedule transactions that take place entirely within such owner's transmission system and do not effect transmission over the systems of other transmission owners. MISO will be responsible for billing and collection for such transmission service. As MISO receives requests for transmission service, MISO also will be responsible for determining whether those requests can be accommodated using the transmission facilities currently under MISO's control or whether an expansion of those facilities would be required. Each transmission owner that is a member of MISO will be responsible for maintaining the transferred transmission assets and implementing any expansion required by MISO, provided that if a transmission owner is financially incapable of implementing an expansion project, the project shall be carried out by other transmission owners or third parties.

1. Modify the way profits, losses and the proceeds from dissolution or sale are divided between the General Partner and the Limited Partners to ensure that the Limited Partners will earn a return based on the amount paid for their investment.
2. Modify the liquidity rights of the General Partner and Limited Partners to restructure in certain respects the liquidity rights of both the General and Limited Partners. For example, these amendments refine the limitations on the rights of the General Partner to initiate an initial public offering of the Partnership or to cause the Partnership to enter into a merger, reorganization or similar kind of corporate transaction that materially changes the business risks to the Limited Partners.
3. Modify slightly the provisions of the Partnership Agreement requiring Limited Partner consent for actions that are outside of the ordinary course of business. These amendments refine the existing consent rights currently held by GE Capital in light of the operating experience and business of the Partnership while continuing to observe the principle that the Limited Partners may not have rights that go beyond the rights normally given to passive investors to protect the value of their investment.
4. Expressly require each partner to maintain non-market participant status and require any partner that becomes a market participant to sell its interest.
5. Make a number of clarifying and technical changes to eliminate inconsistencies and ambiguities in the Partnership Agreement.

Each of these general categories of modifications is described in more detail below.

It is also important to understand the general reason for some of the changes to the Partnership Agreement. The general philosophy behind the changes to the Limited Partner consent rights is to limit the circumstances in which Limited Partner consent to actions by the General Partner is required to cases where the action to be taken by the General Partner is outside the scope of the Partnerships' long-term Business Plan. The Partnership's Business Plan is a brief statement of the general financial goals of the Partnership that sets targets for revenues, EBITDA and capital expenditures. The Business Plan is derived from the five-year plan prepared by Transco and the General Partner. The five-year plan was reviewed in the course of due diligence by the Limited Partners who prepared their own business models and then reconciled the results of their models with the Transco five-year plan. The Business Plan, accordingly, reflects a consensus between the General Partner and the Limited Partners with respect to the general business goals of the Partnership that are reasonably achievable. The goals

set forth in the Business Plan have been deliberately left general to allow the General Partner the most flexibility to achieve these goals.

Similarly, the overall goal of the parties in negotiating the changes to the Partnership Agreement was to leave the General Partner with at least as much discretion over the affairs of the Partnership as it has today. In most instances, this philosophy has resulted in one or more general categories of expenditure or action being eliminated from the category of actions to which the Limited Partners must consent, while at the same time, lowering the dollar threshold at which the Limited Partner consent is triggered. The net effect of these changes has been to more narrowly focus the consent requirements on actions that are outside the scope of the Partnership's Business Plan, leaving the General Partner with significantly greater latitude in many instances, with that additional latitude being offset by slightly more restrictive provisions in the case of actions outside the scope of the Business Plan. Specific aspects of the changes that have been made are discussed below.

#### Amendments to Allocation Provisions

In connection with the Transaction, the Partnership Agreement will be amended to modify the allocation of profits and losses and the proceeds of dissolution or sale of the Partnership among the partners. As modified, the current income of the Partnership will be allocated first to the Limited Partners until the Limited Partners receive a 6% return on their "capital at risk" (defined as the sum of the amount paid by the Limited Partners to purchase their partnership interests plus future capital contributions).<sup>10</sup> All income and losses over the amount of this preferred allocation will be allocated 85% to the Limited Partners and 15% to the General Partner, as is currently the case.

In addition, under the proposed amendments, proceeds from dissolution or sale of the Partnership would be allocated first to the Limited Partners until the Limited Partners receive the return of their "capital at risk" and a 6% return on their capital at risk, with the excess being allocated 85% to the Limited Partners and 15% to the General Partner until the Limited Partners have received an agreed return, and thereafter, 80% to the Limited Partners and 20% to the

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<sup>10</sup> The 6% preference return is currently applicable only with respect to limited partner capital contributions.

General Partner.<sup>11</sup> As was the case in the GE Letter, this negotiated arrangement will continue to provide an economic incentive for the General Partner to manage the Partnership effectively to earn a share of the Partnership's economic return in excess of the value of the General Partner's capital contribution.

#### Liquidity Provisions

In its current form, the Partnership Agreement (i) allows the General Partner to cause the Partnership to enter into a merger or other business combination without the consent of the Limited Partners if the Limited Partners receive an agreed return, and (ii) allows the General Partner to buy out the Limited Partners under certain circumstances if the Limited Partners do not consent to a merger or other business combination that requires their consent.

The amendment modifies the rights of the General Partner to require the Limited Partners to participate in a transaction to which they have not consented under specified circumstances. As modified, the Partnership Agreement will permit the General Partner to require the Limited Partners to participate in an all cash sale of the business provided the Limited Partners receive a minimum return, and will permit the General Partner to buy out Limited Partners that do not consent to participation in a transaction that does not provide for all cash consideration at a price that gives the Limited Partners a required return. In addition, the amendment will give the General Partner limited rights to cause an initial public offering of the Partnership without Limited Partner consent provided that the initial public offering establishes an agreed minimum value for the Limited Partner interests.

The current partnership agreement, in contrast, would permit the General Partner to enter into a merger or other combination if the transaction falls into the category of a Qualified Event. A Qualified Event is a merger or sale of the assets or equity securities of the Partnership or Transco, occurring after the fourth anniversary of the closing date of GE's investment in the

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<sup>11</sup> Under the current Partnership Agreement, on a liquidation, the Limited Partners would receive a return of their capital contributions and a 6% return on that amount, plus an additional \$3,000,000 and an 18% return on that amount, after which the remaining liquidation proceeds would be divided 85% to the Limited Partners and 15% to the General Partner. The proposed amendments will eliminate the additional \$3 million and the 18% return on that amount and the preferred return of 6% will be calculated on the "capital at risk". The 80% - 20% division of the remaining liquidation proceeds, after the Limited Partners have received an agreed return, is new under the amended Partnership Agreement.

Partnership, that is accepted by the limited partner and would yield a certain minimum return to the limited partner. The amended Partnership Agreement dispenses with the "Qualified Event" concept and substitutes instead the concept of a Required Return, defined as, with respect to each Limited Partner, "an amount equal to (i) such Limited Partner's Capital at Risk, plus (ii) a return on the Limited Partner's Capital at Risk at the Required Rate of Return compounded annually from the date on which such Limited Partner's Capital at Risk was put at risk, determined taking into account all Distributions paid to the Limited Partners on or before the date of determination of the Required Return." This is a clearer and more easily administered standard for judging when the General Partner can enter into a merger or other combination without Limited Partner consent.

Because investment liquidity is highly important to a financial investor, the amendment gives the Limited Partners the right to force the sale of the Partnership as a going concern after 2007 if there has been a material failure (defined as a 4.5% (5.5% after 2011) deviation from the business plan<sup>12</sup>) in the performance of the Partnership, or after 2013 even if a material failure has not occurred.

#### Limited Partner Consents

The Partnership Agreement currently contains a number of provisions requiring Limited Partner consent to actions that are out of the ordinary course of business. These provisions provide the Limited Partners with a limited ability to protect their investment without giving them control over the operation of the Partnership's business.

The amendment refines the Limited Partner consent rights in light of the business plan of the Partnership. The principal refinements are:

- The threshold for Limited Partner approval of commitments outside of the Annual Budget has been changed from \$2 million to \$1 million.
- Instead of requiring Limited Partner consent to large asset sales regardless of the reason for the sales, Limited Partner consent is now required only for sales not in the ordinary course of business.

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<sup>12</sup> As discussed below, the amendments will increase this percentage from 2% in the existing Partnership Agreement and the standard by which failure is judged will be modified to include certain regulatory actions.

- The treatment of the Annual Budget has been rationalized to recognize that once adopted, the budget should not be changed.
- The threshold for settling claims against the Partnership without Limited Partner consent has been changed from \$2 million to \$500,000.

Under the current Partnership Agreement, as discussed in more detail below, the General Partner can be removed by the Limited Partners if the Partnership misses its business plan by more than 2% as a result of management decisions over which the General Partner has control. The amendment increases the margin for divergence from the business plan from 2% to 4.5%, initially and then 5.5% after 2011, and redefines the management decisions over which the General Partner is deemed to have control to include adverse regulatory developments.

#### Non-Market Participant Status

Because maintaining the non-market participant status of all investors in the Partnership is critical to the business of the Partnership, the amendment adds a new provision to the Partnership Agreement that requires all partners to maintain non-market participant status or sell their interests.

#### Miscellaneous

The amendment cleans up and clarifies a number of provisions of the Partnership Agreement, particularly with respect to technical tax provisions.

For purposes of completeness, we have described below the roles of the General and Limited Partners in full, and noted the differences between the Partnership Agreement upon which the GE Letter was based (referred to as the existing Partnership Agreement) and the Partnership Agreement as it will be amended in connection with the proposed transaction. In both cases, the General Partner will be responsible for the day-to-day management of the Partnership, and Trans-Elect will be responsible for the day-to-day management of Transco. Under the amended Partnership Agreement, the General Partner will continue to be authorized to do all things that in its sole and reasonable judgment are necessary, proper or desirable to carry out its duties and responsibilities as the General Partner without consulting the Limited Partner. The General Partner will continue to be responsible for activities such as: representing Transco

as a member of a RTO; developing and executing capital expenditure priorities; establishing financial reserves; opening and maintaining bank accounts; drawing checks and handling the Partnership's funds; managing tax matters; and making all elections and determinations contemplated under the Credit Facilities. In addition, as discussed below with respect to the consent rights granted to the Limited Partner, the General Partner has and will continue to have complete discretion concerning certain specified actions, including the incurrence of indebtedness up to \$10,000,000 and any cash sale, merger or other business combination occurring after December 31, 2006 resulting in a specified return to the Limited Partners. The General Partner also has and will continue to have the exclusive right and power to bind the Partnership and to manage and administer the Partnership's business.

Under the Partnership Agreement the consent of the Limited Partners will continue to be necessary with respect to certain extraordinary and other transactions that might materially affect the Limited Partners' investment in the Partnership. The vast majority of these events are identical to the corresponding provisions in the existing Partnership Agreement. To the extent that these provisions have changed, we do not believe that they should change the Staff's view of the status of the Limited Partners under the Act because, as noted above, in virtually all cases the effect of the change has been to give the General Partner greater discretion over actions within the scope of the business plan while offsetting that greater discretion with greater restrictions over actions outside the scope of the business plan. We have indicated below each of the events for which the consent of the Limited Partner will be required under the amended Partnership Agreement and have indicated for each whether it will change from the existing Partnership Agreement and if so, how it will change.

The Limited Partner consent rights in the amended Partnership Agreement will be as follows:

(i) any recapitalization, reorganization, reclassification, merger, consolidation, liquidation, dissolution or other winding up, spin-off, subdivision or other combination, except for certain

sales, mergers or other business combinations occurring after December 31, 2006 resulting in a specified return to the Limited Partners;<sup>13</sup>

(ii) the declaration, setting aside or payment of any dividend or other similar distribution (including a redemption or repurchase of capital) in respect of any class of capital stock of any subsidiary of the Partnership not wholly-owned by the Partnership or by another wholly-owned subsidiary of the Partnership;<sup>14</sup>

(iii) The sale, issuance or redemption of equity securities (or any warrants, options or rights to acquire equity securities or any securities convertible into or exchangeable for equity securities) that might affect the limited partner's interest in the partnership except upon the occurrence of certain events after December 31, 2006 (or December 31, 2005 in the case of an IPO meeting certain conditions).<sup>15</sup>

(iv) the voluntary incurrence of indebtedness by the Partnership or its subsidiaries in the aggregate in excess of \$10,000,000 (A) for borrowed money, (B) evidenced by notes, bonds, debentures or other similar instruments, (C) under capital or financing leases or installment sale agreements or (D) in the nature of guarantees of the obligations described in clauses (A) through (C) of any other person or entity, or the purchase, cancellation or prepayment of, or other provision for, a complete or partial discharge in advance of a scheduled payment date with respect to, or waiver of any right under, any indebtedness of the Partnership or its subsidiaries (whether for borrowed money or otherwise), in either case other than indebtedness of the Partnership or Transco existing under credit facilities as of the closing of the proposed transaction, or indebtedness of a wholly-owned subsidiary thereof;<sup>16</sup>

(v) the entering into or amendment of any contract, agreement, arrangement or commitment with respect to the procurement of goods or services, other than in accordance with the Annual Budget then in effect or as may be reasonably necessary to insure or restore service in the event of a breakdown, service outage or system failure, if any such contract, agreement, arrangement or commitment creates or could reasonably be expected to create a financial obligation in an amount, whether payable at one time or in a series of payments, in excess of \$1,000,000, which consent shall not be unreasonably withheld;<sup>17</sup>

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<sup>13</sup> This provision does not differ substantially from the existing Partnership Agreement, but as noted above under "Liquidity Provisions," both the Limited Partners and the General Partner will have more flexibility with regard to liquidity transactions.

<sup>14</sup> This provision is identical to the corresponding provision in the existing Partnership Agreement.

<sup>15</sup> This provision does not differ substantially from the existing Partnership Agreement. The only difference is in the conditions and timing of an IPO.

<sup>16</sup> This provision is identical to the corresponding provision in the existing Partnership Agreement.

<sup>17</sup> The existing Partnership Agreement provides for Limited Partner consent with regard to "the entering into or amendment of any contract, agreement, arrangement or commitment with respect to the procurement of goods or services, which creates or could reasonably be expected to create a financial obligation in an amount, whether payable at one time or in a series of payments, in excess of \$2,000,000, other than in accordance with the Annual Budget and Business Plan." The amended Partnership Agreement would lower the approval threshold from \$2 million to \$1 million. The amended Partnership Agreement, however, is less restrictive to the General Partner than

(vi) the making of (or committing to make) capital expenditures which either (A) are in an amount greater than \$1,000,000 per event or series of related events (but not otherwise cumulatively) more than the amount contemplated by the Annual Budget or (B) would not be expected to be included in the rate base; provided, however, that neither clause (A) nor (B) shall preclude expenditures that are reasonably necessary to insure or restore service in the event of a breakdown, service outage or other system emergency, which consent shall not be unreasonably withheld;<sup>18</sup>

(vii) the purchase, lease or other acquisition of any securities or assets of any other person, except for acquisitions of securities, products, supplies and equipment in the ordinary course of business consistent with past practice or acquisitions pursuant to the then current annual operating or capital budget and business plan approved in accordance with these consent rights;<sup>19</sup>

(viii) the sale, lease, exchange, Transfer or other disposition of the partnership's, the utility's and their respective subsidiaries' assets or businesses (including, without limitation, the capital stock of any subsidiary) other than (i) sales, leases, exchanges, transfers, or other dispositions in the ordinary course of business, and (ii) the sale of the utility's ownership interest in certain 315kV transmission lines to the Michigan Public Power Agency and Michigan South Central Power Agency to fulfill the utility's obligations under the Midland Antitrust Settlement and the Branch County Settlement pursuant to the terms set out in the existing settlement agreement with respect thereto;<sup>20</sup>

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the existing Partnership Agreement because it would not require Limited Partner consent for commitments with respect to the procurement of goods and services that are reasonably necessary to insure or restore service in the event of a breakdown, service outage or system failure. Such decisions, in particular, are part of managing Transco's business in the ordinary course. In addition, the amended Partnership Agreement provides that Limited Partner consent cannot be unreasonably withheld.

<sup>18</sup> The existing Partnership Agreement provides for Limited Partner consent with regard to "the making of (or committing to make) capital expenditures which are in an amount greater than \$2,000,000 per event or series of related events (but not otherwise cumulatively) more than the amount contemplated by the Annual Budget." The amended Partnership Agreement lowers the approval threshold from \$2 million to \$1 million. However, the amended Partnership Agreement also excludes from the consent requirement any capital expenditures that would be expected to be included in rate base or expenditures that are reasonably necessary to insure or restore service in the event of a breakdown, service outage or other system emergency. Since the vast majority of capital expenditures are anticipated to be included in rate base, the effect of this provision is to give the General Partner significantly more discretion over capital expenditures. The amended Partnership Agreement also will provide that Limited Partner consent cannot be unreasonably withheld.

<sup>19</sup> This provision is identical to the corresponding provision in the existing Partnership Agreement.

<sup>20</sup> The existing Partnership Agreement provides for Limited Partner consent with regard to "the sale, lease, exchange, Transfer, or other disposition of 25% or more of the fair market value of the Partnership's, Opco's and their respective Subsidiaries' assets or businesses on a consolidated basis (including, without limitation, the capital stock of any Subsidiary), as determined by an independent appraiser of national standing." The amended Partnership Agreement would eliminate the 25% of assets threshold, substituting instead an "other than . . . in the ordinary course of business" threshold because such a provision reflects more accurately the view that the General Partner should operate the Partnership in accordance with the agreed business plan. The amended Partnership Agreement also adds a new provision to cover an existing settlement agreement that provides for the sale of certain transmission lines. These sales are already contemplated by the business plan and would therefore not constitute an extraordinary event requiring Limited Partner consent.

(ix) the entering into of any joint venture, partnership or other material operating alliance with any other person;<sup>21</sup>

(x) the making of any material change in accounting practices, except to the extent required by law or generally accepted accounting principals, or voluntarily changing or termination of the appointment of the Partnership's accountants as of the closing of the proposed transaction;<sup>22</sup>

(xi) the commencement of any proceeding or filing of any petition seeking relief under Title 11 of the United States Code, as now constituted or hereafter amended, or any other federal or state bankruptcy, insolvency or receivership or similar law; the consenting to the institution of, or failing to contest in a timely and appropriate manner, any such proceeding or filing; the applying for or consenting to the appointment of a receiver, trustee, custodian, sequestrator, conservator or similar official; the filing of an answer admitting the material allegations of a petition filed against it in any such proceeding; the making of a general assignment for the benefit of creditors; the admitting in writing of its inability, or the failure generally, to pay its debts as they become due; or the taking of any action for the purpose of effecting any of the foregoing;<sup>23</sup>

(xii) the adoption, entering into or becoming bound by, or the amendment, modification or termination of, any (a) employment contract with the executive officers of Transco or the Partnership, including any material change in the compensation or terms of employment of such executive officers, or (b) employee stock option plan or any other material employee benefit plan;<sup>24</sup>

(xiii) the changing of the principal line of business of the Partnership or Transco as in effect on the closing of the Transaction;<sup>25</sup>

(xiv) adoption of any Annual Budget that is inconsistent with the business plan, approval of which shall not be unreasonably withheld. Once adopted, the Annual Budget cannot be amended without the consent of the Limited Partners;<sup>26</sup>

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<sup>21</sup> This provision is identical to the corresponding provision in the existing Partnership Agreement.

<sup>22</sup> This provision is identical to the corresponding provision in the existing Partnership Agreement.

<sup>23</sup> This provision is identical to the corresponding provision in the existing Partnership Agreement.

<sup>24</sup> This provision is unchanged from the corresponding provision in the existing Partnership Agreement, except that it now provides that consent shall not be unreasonably withheld.

<sup>25</sup> This provision is identical to the corresponding provision in the existing Partnership Agreement.

<sup>26</sup> The existing Partnership Agreement provides for Limited Partner consent with regard to "the adoption of any change in an Annual Budget (while it is effective) of more than 15% in the aggregate or the adoption of any Annual Budget that is inconsistent with the Business Plan." The amended Partnership Agreement does not include a 15% budget change threshold. The budgeting process under the amended Partnership Agreement is based on the premise that major expenditures should be considered as part of an overall budget. Capital expenditures for a transmission business are the result of a very long-term planning process that requires the involvement of numerous parties. Once the Annual Budget is adopted by the General Partner, which does not require investor consent if it is consistent with the long-range business plan, the Annual Budget establishes the spending plan for the year, and in the absence of special circumstances, unbudgeted expenditures should be considered when the budget for the next year is established. This approach encourages management to conduct its planning on an appropriately long-term basis and, consistent with good management policy, requires major expenditure decisions to be considered as part of the

(xv) the exercising of its right to vote the membership interests (or similar equity interest) of any subsidiary of the Partnership in extraordinary circumstances, including, without limitation, mergers, sales of significant assets or changes in organizational or charter documents;<sup>27</sup>

(xvi) the effectuation of a public offering or private sale or other change of control (other than financing activities in the ordinary course);<sup>28</sup>

(xvii) the entering into of any transaction involving conflicts of interest between the Partnership and the General Partner or any affiliate of the General Partner (including employees and directors of the General Partner and its affiliates), or the payment by the Partnership of any fees or other amounts to the General Partner or any affiliate of the General Partner;<sup>29</sup>

(xviii) the amendment or modification of the Partnership's, the General Partner's or any of the Partnership's subsidiaries' organizational documents so as to change the powers, preferences or special rights of the Limited Partner or in a manner that would otherwise adversely affect the rights of holders of limited partnership equity;<sup>30</sup>

(xix) the filing of any application to obtain, or any material amendment to, a material governmental permit or approval, or any material filing in connection with a Transco rate proceeding or any material change to the rates or other charges under any Transco tariff;<sup>31</sup>

(xx) the settlement or compromise of any action, suit, claim, dispute, arbitration or proceeding that would materially adversely affect the partnership or any of its subsidiaries or require the payment of more than \$500,000 in the aggregate;<sup>32</sup>

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overall budgeting process, and not on a piecemeal basis. If, after an Annual Budget is adopted, changed circumstances make it desirable to consider unbudgeted expenditures before the next year's budget cycle, the General Partner has complete discretion to make any expenditures necessary to deal with outages and other emergency situations and to make capital expenditures that are included in rate base without Limited Partner consent. These expenditures clearly enhance the value of the transmission system and will generally encompass the vast majority of capital expenditures that Transco is expected to make. The only unbudgeted expenditures that require Limited Partner consent if not considered as part of the Annual Budget process are expenditures that are not necessary or appropriate to maintain or enhance the transmission system and exceed limits that are well within the established precedent for requiring investor approval.

<sup>27</sup> This provision is identical to the corresponding provision in the existing Partnership Agreement.

<sup>28</sup> Although this provision is identical to the corresponding provision in the existing Partnership Agreement, other provisions of the amended Partnership Agreement have been modified to permit the General Partner to undertake an IPO of partnership interests without the consent of the Limited Partners in some circumstances where consent would be required under the existing Partnership Agreement.

<sup>29</sup> This provision is identical to the corresponding provision in the existing Partnership Agreement.

<sup>30</sup> This provision is identical to the corresponding provision in the existing Partnership Agreement.

<sup>31</sup> This provision is identical to the corresponding provision in the existing Partnership Agreement.

<sup>32</sup> The existing Partnership Agreement provides for Limited Partner consent with regard to "the settlement or compromise of any action, suit, claim, dispute, arbitration or proceeding that would materially adversely affect the Partnership or any of its Subsidiaries or require the payment of more than \$2,000,000 in the aggregate." The amended Partnership Agreement is identical except that the consent threshold would be lowered to \$500,000. The Limited Partners' ability to give its consent with regard to the settlement of litigation is unlikely to have a material influence on management behavior due to the relative infrequency of significant litigation arising. Considering the

(xxi) any action (or failure to act) by the Partnership or any of its subsidiaries that would result in the Limited Partner or its affiliates (other than the Partnership and its subsidiaries): (a) being subject to regulation as a "holding company" or a "subsidiary company" or an "affiliate" of a "holding company" or a "public-utility company" under the Act or (b) being subject to any other federal or state regulation that in the Limited Partner's reasonable discretion would have an adverse affect on the Limited Partner or any such affiliate,<sup>33</sup> or

(xxii) the entering into of any contract, agreement, arrangement or commitment to do or engage in any of the foregoing.<sup>34</sup>

The amended Partnership Agreement also will add a new provision to allow the Limited Partners to call a meeting of the Partnership's partners if such partners have not met in the last four months. In addition, the Partnership Agreement will be amended to require that the General Partner cause Transco to carry and maintain insurance coverage satisfactory to the Limited Partner.

Finally, the amended Partnership Agreement will provide that the General Partner may be replaced for "cause," where "cause" is defined to include: (i) gross negligence or willful misconduct, (ii) failure to comply in any material respect with any applicable law or regulation (including environmental law) or (iii) any "controllable management decision" by the General Partner that in the reasonable judgment of the Limited Partner has resulted in, or will result in, a "material failure" to achieve the Partnership's business plan. The General Partner also may be removed if it becomes a market participant and such status has an adverse effect that is material to the Partnership or Transco.<sup>35</sup>

A "controllable management decision" is defined in the Partnership Agreement as the performance, taking, failure to perform or take or omission of any action by the General Partner, Trans-Elect or any other person acting under the direct or indirect management or control of the General Partner or Trans-Elect; provided, however, that the following events shall not constitute "controllable management decisions": (i) the effects on financial results due to changes in law;

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increased operational latitude granted to the General Partner in other sections of the amended Partnership Agreement, the lower threshold for litigation settlements does not represent a significant restriction on the General Partner's discretion over the day-to-day management of the Partnership.

<sup>33</sup> This provision is identical to the corresponding provision in the existing Partnership Agreement.

<sup>34</sup> This provision is identical to the corresponding provision in the existing Partnership Agreement.

<sup>35</sup> This provision is the same as the existing Partnership Agreement, except for the ability to remove the General Partner if it becomes a market participant.

(ii) changes in demand for transmission services; and (iii) other similar factors beyond the control of management. For purposes of this definition, (A) the effect of actions of regulators specifically applicable to Trans-Elect and Transco, but not the effect of determinations by regulators of policies applicable to owners or operators of transmission systems generally, shall be deemed to be the result of a controllable management decision and (B) the General Partner shall not be deemed to have anticipated the timing of regulatory filings made by third parties or the timing of the issuance of orders that would not reasonably be anticipated by a person who is knowledgeable in such regulatory matters.<sup>36</sup>

A "material failure" is defined under the Partnership Agreement as any actual failure to achieve the EBITDA contemplated by the Business Plan by an average of 4.5% or more during any period of two consecutive Partnership Years ending prior to January 1, 2011, and an average of 5.5% during any period of two consecutive Partnership Years thereafter. For purposes of determining whether a Material Failure has occurred, the effect on EBITDA of changes in the amortization period of any capital expenditure deferral shall be disregarded provided that the amortization period does not exceed 12 years.<sup>37</sup>

There is one final change to the Partnership Agreement that is being made that should be noted here, although we do not believe that it has any effect on the analysis of the Limited Partners' status under the Act. Certain of the Limited Partners are required to preserve their status as "venture capital operating companies" ("VCOC") as defined in 29 C.F.R. Section 2510.3-101(d)(3)(i), the regulations promulgated under the Employee Retirement Income Security Act ("ERISA"). In order to assure compliance with these requirements, the Partnership has agreed that upon request it will grant to a Limited Partner certain rights which are designed to ensure that the Limited Partner maintains its status as a VCOC.<sup>38</sup> Although required by

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<sup>36</sup> The only change to the amended provision makes management more accountable for the effect of actions of regulators specifically applicable to Trans-Elect and Transco, but not with respect to the effect of determinations by regulators of policies applicable to owners and operators of transmission systems generally.

<sup>37</sup> Notably, the Partnership Agreement increases the threshold for a material failure from 2% (based on cumulative EBITDA with a one-year cure right), under the existing partnership agreement to 4.5% initially and later 5.5% (based on annual EBITDA over an average of two fiscal years without a cure right) under the amended Partnership Agreement. This more flexible standard should provide the General Partner with a greater ability to cure deviations from the Business Plan.

<sup>38</sup> These rights include (i) the right to visit and inspect any of the offices and properties of the Partnership and inspect and copy the books and records of the Partnership, (ii) the right to receive GAAP financial statements of the

ERISA regulations, we do not view the possibility that these rights may be granted to certain of the Limited Partners as having any effect on the Limited Partners' status under the Act. Many of the rights are nothing more than rights to obtain information that a limited partner already has under state law. The others are rights of *consultation* (but not approval as is the case with the consent rights under the Partnership Agreement) with respect to the very same issues that are the subject of the consent rights specified in great detail in the Partnership Agreement and discussed above. In our view, the VCOC rights are necessary for purposes of ensuring compliance with applicable ERISA regulations, but do not change the fundamental nature of the Limited Partners' status as passive investors.

#### 4. The Preferred Stock Investment in Trans-Select

The Limited Partners will acquire GE Capital's interest in 25% of the shares of Trans-Select's Series C Preferred Stock, which represents approximately 12.5% of Trans-Select's outstanding equity.<sup>39</sup> The Series C Preferred Stock is convertible at the holder's option into common stock of Trans-Select. As was the case with GE Capital, the Limited Partners will

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Partnership, (iii) the right to receive any annual reports, quarterly reports and other periodic reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934, actually prepared by the Partnership as soon as available, (iv) the right to receive copies of all materials provided to the limited partners of the Partnership. In addition, the VCOC rights require the Partnership to (i) make appropriate officers and/or directors of the Partnership available periodically and at such times as reasonably requested by the VCOC Entity for consultation with the VCOC Entity or its designated representative with respect to matters relating to the business and affairs of the Partnership, (ii) inform the VCOC Entity or its designated representative in advance with respect to any significant corporate actions, including, without limitation, extraordinary dividends, mergers, acquisitions or dispositions of assets, issuances of significant amounts of debt or equity and material amendments to the certificate of incorporation or by laws of the Partnership, and to provide the VCOC Entity or its designated representative with the right to consult with the Partnership with respect to such actions, (iii) provide the VCOC Entity or its designated representative with such other rights of consultation as may reasonably be determined by the VCOC Entity to be necessary to qualify its investment in the Partnership as a "venture capital investment" pursuant to the Plan Asset Regulation, and (iv) to consider, in good faith the recommendations of the VCOC Entity or its designated representative in connection with the matters on which it is consulted as described above.

<sup>39</sup> The Limited Partners will acquire the Series C Preferred Stock in the same proportion that they acquire Limited Partnership interests. The Limited Partnership interests and the number of shares of stock acquired would be as follows:

Investor	Percentage of Limited Partnership Interest	Number of Shares of Stock
EMI	43.636%	17,455
EMC	1.818%	727
MTM	21.212%	8,485
NA Holdings	21.212%	8,485
Mich 1400	12.121%	4,848

irrevocably give up voting rights applicable to those shares for so long as they or any affiliate owns them (except for the right to vote with respect to certain consent rights described below) and will give up the right to appoint a director to Trans-Elect's Board of Directors in exchange for the right to designate up to two non-voting observers to such Board. No Limited Partner would be permitted to designate more than one observer. The consent rights applicable to the shares held by the Limited Partners will be identical to those held by GE Capital and will be limited to the following types of extraordinary events that might affect the interests of the holders of the Series C Preferred Stock: (i) changes to Trans-Elect's Articles of Organization or By Laws, (ii) a merger, consolidation or substantial asset acquisition, (iii) a redemption or repurchase of stock, (iv) a sale or other disposition of a material portion of Trans-Elect's assets other than in the ordinary course, (v) changes in accounting or financial policies, (vi) issuance or other authorization of securities ranking on a parity with or senior to the Series C Preferred Stock, (vii) issuance of stock that would dilute the interests of the Series C Preferred Stock, (viii) amendment of employee option or benefits plans, or (ix) approving or modifying agreements with officers, directors or other affiliates. These consent rights, which are similar to rights granted to debt holders, were intended to give the passive investors in the Series C Preferred Stock the ability to vote, as a group, with respect to certain extraordinary events that might irrevocably affect the rights or preferences associated with their interest in Trans-Elect. The Limited Partners will own only 25% of the shares of the Series C Preferred Stock and any required consent with respect to that stock will have to be approved by a majority of the shares of the Series C Preferred Stock voting as a class. Accordingly, the Limited Partners will have no ability to veto any event requiring such consent.

## **II. Issues Arising Under the Act**

The Partnership owns all of the limited liability company interests in Transco and is a "holding company" as defined in Section 2(a)(7) of the Act. As a holding company, the Partnership qualifies for an exemption from registration pursuant to Section 3(a)(1) of the Act because the Partnership and Transco are predominantly intrastate in character and they carry on their business solely within Michigan, which is the state in which both the Partnership and Transco are organized. In addition, as the general partner of the Partnership, TE Michigan (and

its parent, Trans-Elect) also are "holding companies" and each qualifies for an exemption under Section 3(a)(1) of the Act.<sup>40</sup>

For the reasons described below, it is our opinion that, as a result of the Transaction, none of the Limited Partners should be deemed to be a "holding company" or an "affiliate" (as such terms are defined in Sections 2(a)(7) and 2(a)(11)(A) of the Act, respectively) of the Partnership, Transco or any of their subsidiaries because the Limited Partners would not (A) directly or indirectly, own, control or hold with the power to vote "voting securities" of a public utility company or of a holding company, as the term "voting securities" is defined in Section 2(a)(17) of the Act, or (B) exercise "a controlling influence over the management or policies" of a public utility or of a holding company such that regulation is required under the Act.

#### A. The Limited Partnership Interest and the Non-Voting Preferred Stock are Not Voting Securities

A "voting security" is defined in Section 2(a)(17) of the Act as "any security presently entitling the owner or holder thereof to vote in the direction or management of the affairs of a company." The Commission has issued a number of no-action letters supporting our conclusion that the consent rights associated with the Limited Partners' interest in the Partnership and the Limited Partners' non-voting preferred stock interest in Trans-Elect do not cause those interests to be considered "voting securities" under the Act. See e.g., General Electric Capital Corp., (April 26, 2002); k1 Ventures, et al., (July 28, 2003); SW Acquisition, L.P. (April 12, 2000); Berkshire Hathaway, Inc. (March 10, 2000); Torchmark Corp. (January 19, 1996); Commonwealth Atlantic L.P. (November 30, 1991); Nevada Sun-Peak L.P. (May 14, 1991); and John Hancock Mutual Life Ins. Company (July 23, 1986). In this series of no-action letters, the Staff has identified numerous types of consent rights that do not cause the holder of such rights to have a vote in the direction or management of the underlying holding company or utility. Instead, the Staff has recognized that these consent rights are intended to protect the investment of the limited partners or preferred shareholders, similar to the rights granted to debt holders by

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<sup>40</sup> TE Michigan is a Michigan limited liability company, and Trans-Elect is incorporated in Michigan. The Partnership, TE Michigan and Trans-Elect have filed annual reports with the Commission on Form U-3A-2 confirming that each such holding company, and every utility subsidiary from which such holding company derives a material part of its income, is predominantly intrastate in character and carries on its business substantially in Michigan.

means of negative covenants in debt instruments. The consent rights granted to the Limited Partners and to the holders of Trans-Elect's Series C Preferred Stock fall squarely within the boundaries outlined in prior no-action letter requests.<sup>41</sup>

For instance, in Torchmark Corp., the Staff confirmed the position taken by the applicant that a limited partner with 47.5% of the total equity of the partnership would not be deemed to hold voting securities in the partnership (and thus would not be deemed a holding company or an affiliate of the natural gas distribution company that was owned by such partnership), despite the considerable consent rights granted to its limited partners. In that case, the limited partners were granted consent rights concerning: (i) any sale, exchange, lease, mortgage, or other disposition of 25% or more of the fair market value of the partnership's business or assets, (ii) any merger, takeover, consolidation or similar business reorganization, (iii) the issuance or prepayment of debt (including guarantees) in excess of \$1,000,000 other than in the ordinary course of business, (iv) settling a dispute or litigation in an amount in excess of \$1,000,000 other than in the ordinary course of business, (v) admitting any additional limited or general partner, (vi) dissolution, winding up or liquidation, (vii) commencement of (or acquiescence in) a bankruptcy petition, (viii) entering into or amending any material provision of any material contracts, (ix) any capital expenditure in excess of \$500,000, (x) amending any material governmental permit or filing or seeking governmental action other than in the ordinary course of business, and (xi) adopting or modifying the partnership's budget to result in an increase of 15% for any category or expense. This list of consent rights expanded upon the consent rights described in prior no-action letter requests and provided the limited partners with significant protections from adverse actions by the partnership with respect to financial matters, extraordinary corporation transactions and events, as well as potential conflicts with the general partner.

Recently, in SW Acquisition, L.P., the Staff concurred with the opinion that the limited partnership interests described in that request did not constitute "voting securities" based on factual circumstances similar to those set forth in this letter. In SW Acquisition, L.P., the limited partners held 99.9% of the equity of the partnership, with the largest limited partner owning a

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<sup>41</sup> Please note, these rights are also consistent with the types of consent rights granted to preferred stockholders under the Commission's former "Statement of Policy Concerning Preferred Stock."

24.38% interest, and the limited partners were granted consent rights concerning a wide variety of events.<sup>42</sup> The consent rights to be granted to the Limited Partners under the amended Partnership Agreement closely match the consent rights held by the limited partners in SW Acquisition, L.P. and the consent rights held by owners of Trans-Elect's Series C Preferred Stock are significantly less extensive.

The most recent instance in which the Staff concurred that non-managing member consent rights similar to the consent rights held by the Limited Partners did not constitute voting securities was in k1 Ventures. Like the current transaction, the k1 Ventures non-managing members had consent rights with respect to fundamental organizational issues, major operational issues, interested party transactions and with respect to regulatory status under the Act. All of these rights had in common the preservation of the investment expectations agreed to by the managing member and non-managing members during the term of the non-managing members' investment.<sup>43</sup>

The Limited Partners have also agreed to enter into an agreement (the "Investors Agreement") pursuant to which they have agreed to vote among themselves with respect to how their Limited Partnership Interest should be voted under the Partnership Agreement.<sup>44</sup> Under the Investors Agreement, the Limited Partners have agreed that certain consents will require a higher

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<sup>42</sup> In particular, the limited partners in SW Acquisition, L.P. held consent rights concerning the approval of: (i) distributions under the partnership agreement, (ii) a public offering of the securities of the partnership or its subsidiaries, (iii) changes in the aggregate of greater than 15% to the business plan and annual operating budget, (iv) contracts for goods and services, or the incurrence of indebtedness, in excess of \$1 million, except in accordance with the current business plan and annual budget, (v) mergers, joint ventures, partnerships and similar transactions, (vi) capital expenditures that vary from the current budget by \$5 million or more, (vii) material changes in accounting practices or a change of the partnership's accountant, (viii) initiating actions or suits in excess of \$1 million, and (ix) adopting material employee benefits plans or employment agreements.

<sup>43</sup> For example, the non-managing member retained the right to consent to the entry into contracts for goods and services in excess of \$300,000, other than in accordance with the annual business plan and operating budget, capital expenditures that exceed budgeted amounts by \$750,000 or more, the settlement of suits or arbitration in excess of \$500,000, and the entry into any agreement or arrangement that is not in the ordinary course of business other than as expressly permitted by the budgets. The thresholds for the relevant consent rights in the proposed transaction are comparable when the Limited Partners' investment at risk is compared to the size of the investments in the k1 Ventures and SW Acquisition, L.P. transactions.

<sup>44</sup> Under the Investors Agreement, the Limited Partners have agreed to vote their Partnership Interests as a block with respect to any votes required to be taken under the Partnership Agreement based on the results of a prior vote taken among the Limited Partners. The required vote varies depending on the action to be taken, ranging from approval of Limited Partners holding 55% of the Limited Partnership Interests up to 90%. Therefore, one or more of the Limited Partners could veto certain approvals by voting against it. Nevertheless, with the exception of certain liquidity and capital contribution transactions, no consent could be given by a single Limited Partner.

Limited Partner approval threshold than is otherwise required under the Partnership Agreement. Under these circumstances, we do not believe that the voting arrangements among the Limited Partners should have any affect on the staff's analysis because the level of influence that an individual Limited Partner has over the actions of the General Partner and the Partnership are considerably more diffuse than is presently the case with a single Limited Partner holding all of the Limited Partnership Interests. Given that the Limited Partnership Interest is moving from being under the control of a single entity (GE) into the control of four independent investors, it is hard to see how they could be deemed to have a higher degree of control than the single owner from which they are acquiring their interests even if they have agreed to enter into the Investors Agreement. In any event, on several occasions the Staff has issued no-action letters in response to requests by limited partners with significant consent rights, irrespective of the fact that the consent of a single limited partner (as opposed to a group of unrelated partners) was necessary to approve the applicable events covered by such consent rights. See e.g., Nevada-Sun Peak L.P. (consent of single limited partner required for extensive list of "major business decisions"); Dominion Resources, Inc. (Jan. 21, 1988) (consent of single limited partner required for specified "major events"); Accord, Berkshire Hathaway, Inc. (consent of corporation holding preferred shares required for specified actions).<sup>45</sup>

Finally, the fact that the shares of Trans-Elect's Series C Preferred Stock, are convertible into voting interests under certain circumstances does not cause such limited partnership interest or non-voting preferred stock to be considered a "voting security" under the Act prior to such conversion. In numerous instances, the Commission and the Staff have respected the fact that convertible securities are not voting securities until such time as they are converted into securities with voting rights.<sup>46</sup> The Limited Partners will not rely upon the assurances granted in connection with this no-action letter request after the date of such conversion, unless the Limited Partners receive further assurances from the Staff.

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<sup>45</sup> As discussed above, the Limited Partners have no ability to use their consent rights as holder of Trans-Elect's Series C Preferred Stock to veto any event requiring such consent because the Limited Partners own only 25% of the shares of the Series C Preferred Stock and any required consent with respect to that stock may be approved by a majority of the shares of the Series C Preferred Stock voting as a class.

<sup>46</sup> See e.g., Pinnacle West Capital Corp. (Feb. 7, 1990) ("The two salient features of the definition of a 'voting security,' therefore, are (i) that it provides the owner or holder thereof with a present right to vote; and (ii) that such present right to vote may be exercised in the direction or management of the affairs of a company.")

For these reasons, it is our view that the consent rights to be held by the Limited Partners should not cause the interests they will hold directly or indirectly in the General Partner or the Partnership to be deemed to be "voting securities."

B. The Limited Partners will not exercise such a Controlling Influence over the Partnership or Transco that Regulation would be Required under the Act

Under Section 2(a)(7) of the Act, the owner of 10% or more of the voting securities of a holding company or a public-utility company is presumed to control such holding company or public utility company and thus such owner is presumed to be a holding company.<sup>47</sup> Alternatively, the owner of less than 10% of the voting securities of a holding company or a public-utility company is not presumed to control such holding company or public-utility company unless the Commission determines, after notice and opportunity for hearing, that such owner exercises such a controlling influence over the holding company or public-utility company in question that the Commission finds it necessary or appropriate to regulate the owner as a holding company under the Act.

We believe that the structure and terms of the Limited Partners' investment in the Partnership, as well as the Limited Partners' non-voting preferred stock interest in Trans-Elect, evidence the fact that the Limited Partners will not have such controlling influence over the management or policies of the General Partner, the Partnership or Transco that regulation under the Act is required. Our opinion is bolstered by the facts and arguments relied upon in prior no-action letter requests granted by the Staff, and in particular the GE Letter, since the structure of the Transaction is essentially the same in every material respect to the GE Capital investment. As the comparison in Section I.B.3 above demonstrates, the terms of the Limited Partners' investment in the Transaction also will be very similar to the terms enjoyed by GE Capital. To the extent that the provisions that were applicable in the GE Letter have been modified, we believe that they are within the parameters for consent rights to which the Staff has acquiesced in other letters, including the recently issued k1 Ventures letter. For example, the non-managing members in k1 Ventures have consent rights with respect to the offering of debt securities or

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<sup>47</sup> The owner of 10% or more the voting stock of a utility may overcome this presumption of control under certain circumstances.

other voluntary incurrence of indebtedness in excess of \$300,000. In contrast, the Limited Partners' consent rights in similar circumstances will be triggered by the issuance of indebtedness in excess of \$10 million. The k1 Ventures non-managing members also have consent rights with respect to the entry of the LLC into contracts for goods and services in excess of \$300,000. In contrast, the Limited Partners' consent rights in similar circumstances will be triggered by transactions in excess of \$1 million. A comparison of the approval rights with respect to capital expenditures also indicates that the Limited Partners' approval rights will not be more extensive than deemed acceptable in k1 Ventures. In k1 Ventures, the non-managing members have consent rights with respect to capital expenditures that vary from budgeted amounts by \$750,000 or more. The Limited Partners' consent rights in similar circumstances will be triggered at the \$1 million level. Lastly, the consent threshold for the settlement of suits and other disputes will be \$500,000; the same for both k1 Ventures' non-managing members and the Limited Partners. The relevant consent thresholds in the Transaction are comparable when the Limited Partners' investment at risk is compared to the size of the k1 Ventures and SW Acquisition, L.P. transactions.

The determination of whether a party has a "controlling influence" is a judgment to be made by the Commission based on the facts of a particular case. In the past, the Commission has relied on the following facts and circumstances in making its determination: "(i) the terms and provisions of the securities that create the relationship, (ii) whether there are agreements between those with voting control and others who have invested in the company, (iii) any past or present business relationship between the entities with voting control and the company and (iv) the nature of the parties involved, including whether there is capable, independent and financially interested management to operate the public utility and holding company." (Berkshire Hathaway, Inc.)

As shown above, the consent rights to be held by the Limited Partners, and the consent rights held by the shareholders of Trans-Elect's Series C Preferred Stock, are consistent with the rights granted to other similar investors that have received no-action letter assurances. Although the Limited Partners will vote their partnership interests jointly under the Investors Agreement, the net result of such collaboration is that they will have no more control than was possessed by

GE Capital which has held all of the limited partnership interests in the Partnership as a block. We consider it important, however, that there will be no voting agreements between the Limited Partners and the General Partner or the Partnership. Furthermore, as discussed below, independent individuals with significant qualifications and experience will be in control of the management of the General Partner, the Partnership and Transco.

The Limited Partners have no ability to control the management or day-to-day operations of the Partnership or Transco. The Partnership Agreement will provide that the General Partner has the exclusive right to control the business of the Partnership. The Limited Partners are passive investors with merely an economic interest in such entities. The Limited Partners have no rights under the Partnership Agreement, and will not otherwise attempt, to control the daily operations of the Partnership or Transco.

The Limited Partners' ability to vote with respect to the limited consent rights granted to owners of Trans-Elect's Series C Preferred Stock will not give the Limited Partners the ability to control or influence Trans-Elect in such a way that the Limited Partners should be considered to share control over the management or operations of the General Partner or the Partnership. As minority investors in Trans-Elect's Series C Preferred Stock, the Limited Partners and the other passive investors in Trans-Elect will hold only limited consent rights exercisable as a group. Those rights, which are similar to the consent rights retained by classes of debt holders, are necessary to help protect such investors from extraordinary events outside of the ordinary course (such as the sale of a material portion of assets, or an issuance of securities in parity or senior to the interests of the preferred stock) that might adversely affect the rights or preferences of such investors. Because the Limited Partners own only 25% of the shares of the Series C Preferred Stock and any required consent with respect to that stock may be approved by a simple majority, the Limited Partners cannot veto any action by Trans-Elect. Thus, these limited consent rights will not give the Limited Partners any additional control or influence over the Partnership, which is a distinct and separate entity.<sup>48</sup>

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<sup>48</sup> Simply stated, if a transaction requires Limited Partner consent under the consent rights described above, then the Limited Partners would be able to prevent the requested action of the Partnership by withholding their consent. However, even if a particular transaction were to require the consent of both the holders of the Series C Preferred Stock and the Limited Partners (such as an acquisition requiring significant securities issuances by both Trans-Elect

We note that Macquarie Securities (USA) Inc. ("Macquarie Securities"), a wholly owned subsidiary of Macquarie Holdings (USA), is a financial advisor to Trans-Elect. In that capacity, Macquarie Securities provides consulting and advisory services with respect to financings and potential acquisitions to Trans-Elect for a fee. Macquarie Securities has been selected to provide these services pursuant to the sole discretion of Trans-Elect and the advisory and consulting services do not relate to Trans-Elect's management of Transco or the Partnership. Moreover, in the future, Macquarie Holdings (USA) expects to either sell NA Holdings to one or more unaffiliated investors or to transfer NA Holdings to a fund managed by another member of the Macquarie group.<sup>49</sup> In addition, our view of MEAP's status under the Act is not affected by MEAP's investment in AltaLink. MEAP has no ability to control AltaLink, and even if it did, such control would not give it a controlling influence over the Partnership.<sup>50</sup>

We also note that MP Structured Finance Fund ("MPSFF") has made a loan to the General Partner in the original principal amount of \$3,500,000 that is secured by the General Partner's interest in the Partnership. MPSFF is a Bermuda Unit Trust in which the Macquarie group has a minority interest. The Macquarie group is entitled to appoint one of the three directors of the trustee and owns 50% of the manager of MPSFF. Another minority investor is entitled to appoint one of the other two directors and also owns 50% of the manager. The third director is independent as required under Bermuda law. Most significant management decisions at MPSFF require the unanimous consent of the director appointed by the Macquarie group and the director appointed by the other minority investor. In connection with the Transaction, a portion of the loan to the General Partner will be repaid. Although the terms of the loan contain

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and the Partnership), the Limited Partners would not be able to prevent an issuance by Trans-Elect because the Limited Partners would hold only a minority interest in the Series C Preferred Stock. See John Hancock Mutual Life Ins. (no-action letter issued in response to request stating that a limited partner's ownership of equity and debt securities of the general partner of the utility project do not constitute a "material interrelationship, such as an interlocking directorship or a material contractual relationship" that would give the limited partner a "controlling influence" over the partnership); Contrast Kaufman and Broad, Inc. (April 17, 1985) (declining to issue the requested no-action letter assurances to a limited partner because of the concern that Eli Broad, who was the president of the general partner and owned nearly one-third of the limited partnership shares, could control the votes of both the general and limited partners).

<sup>49</sup> Macquarie does not intend to transfer NA Holdings to MPSFF (as defined below).

<sup>50</sup> MEAP, a Canadian limited partnership, is managed by its general partner, which is compensated based on the capital invested by MEAP and the performance of the investment portfolio. The general partner of MEAP is a subsidiary of Macquarie Bank. The performance of the AltaLink investment is separate and apart from the performance of MTM's investment in the Partnership.

customary covenants designed to protect the lender against actions of the borrower that could adversely affect the lender, we do not view the relationship as affecting the status of the Limited Partners under the Act. MPSFF is separately managed from NA Holdings and, in any event, MPSFF rights as a lender relate to activities that the General Partner may undertake on its own behalf, not actions that the General Partner may take on behalf of the Partnership in its capacity as General Partner.

The MPSFF loan was made prior to the negotiations related to the Transaction and is independent of the Transaction. Macquarie Bank and its affiliates have no intention of making future loans to the General Partner and they are aware that any additional loans could affect the Limited Partners' ability to rely on the relief sought in this letter. The Macquarie group will not use its interest in MPSFF and the MPSFF loan to exert a controlling influence over the General Partner, provided however, that MPSFF would not be restricted from enforcing its rights as a lender under the loan documents to the extent that it does not take actions or assert rights that would result in the exercise of a controlling influence over the General Partner.

Similarly, we do not view the fact that KBRWJ LP is also a passive investor in the Path 15 Transmission project to affect Mich 1400's status under the Act. Neither of these relationships gives either passive investor any additional level of control or influence over the Partnership and in our view does not affect the analysis under the Act.

It is important to recognize, as was the case in SW Acquisition, L.P., that the General Partner is a substantive company that provides experienced management in the operation of Transco. Under the Partnership Agreement, the General Partner will continue to have full control to operate and manage the business affairs of the Partnership, including representing Transco as a member of a RTO; developing and executing capital expenditure priorities; establishing financial reserves; opening and maintaining bank accounts; drawing checks and handling the Partnership's funds; managing tax matters; and making all elections and determinations contemplated under the Credit Facilities.

The General Partner will continue to be controlled by individuals independent of the Limited Partners with a significant economic interest in the continued success of the Partnership and Transco. As in SW Acquisition, L.P., the vested economic interest of the General Partner is

potentially much greater than its capital contribution. Based on negotiations between the parties and consideration of their respective roles, the Partnership Agreement grants to the General Partner the right to receive participating distributions in an amount equal to 15% of the adjusted cash flow received from Transco from its operations remaining after payment of the "preference distribution," certain capital expenditures and debt service. Thus, the General Partner will continue to have a substantial incentive to effectively manage the operations of the Partnership and Transco.<sup>51</sup> This division of economic benefits, the consent rights described above and the other aspects of the Partnership Agreement are the result of detailed arm's-length negotiations among the parties. Furthermore, as the GE Letter notes, the individuals that will manage the Partnership and Transco are well-known and experienced executives and managers in the utility industry, and are more than qualified to oversee the operations of the utility and to hire qualified managers and employees.

Under the Partnership Agreement, the Limited Partners will have no right to appoint or otherwise nominate any members of management of the Partnership or Transco. Based on its minority, preferred shareholder interest in Trans-Elect, the Limited Partners will have the right to send up to two non-voting observers to meetings of Trans-Elect's Board of Directors. This same arrangement was present in the GE Letter. In contrast, in prior no-action letters, the Staff has given assurances to passive investors that were granted the right to appoint one or more voting members to the Board of Directors of a holding company or a public-utility company. The ability to have such representation has been supported in no-action letter requests as necessary to permit the passive investor to monitor the activities of the entity in which it has invested, without giving the investor the right to veto or otherwise manage or control the operations of such entity. Western Resources, Inc. (Nov. 24, 1997) (granting owner of common and preferred stock representing approximately 45% of utility's equity the right to appoint two of the utility's fifteen directors); Ocean State Power<sup>2</sup> (Feb. 16, 1988) (granting each of the six partners a representative to the partnership's management committee). As stated in Torchmark Corp., the Limited Partner

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<sup>51</sup> In practice, the general partner of a limited partnership is typically entitled to a smaller economic interest than the limited partners, who often finance the majority of the equity investment of the partnership. However, this disparity in economic interest has not prevented the Staff from issuing no-action letters to such limited partners concerning enforcement of the Act. See, e.g., SW Acquisition, L.P.; Torchmark Corp.; Commonwealth Atlantic L.P.; Nevada Sun-Peak L.P.; and John Hancock Mutual Life Ins. Company.

is not required to be "a stranger to the organization of the Partnership" as long as its involvement is limited to protecting its investment.

In addition, in the no-action letter involving Berkshire Hathaway, Inc., the Staff indicated that it would not recommend that the Commission find that Berkshire Hathaway would have a "controlling influence" over the holding company acquired in that transaction despite the fact that Berkshire Hathaway would own approximately 81% of the holding company's total equity, including approximately 9.7% of its voting stock and the remainder in convertible preferred stock (which entitled it to appoint two of the holding company's ten directors and to exercise consent rights with respect to certain extraordinary actions). While it is recognized that the rights of the Limited Partners in the Partnership (like Berkshire Hathaway's consent rights as a preferred shareholder) may be used to withhold consent as to any transaction or event within their scope, any leveraging of those rights to obtain more expansive agreements or understandings relative to the direction of the management of the Partnership or Transco could, without further assurances from the Staff, subject the Limited Partners to regulation as a holding company or an affiliate under the Act.<sup>52</sup>

As in SW Acquisition, L.P., the Partnership Agreement will grant to the Limited Partners a limited right to replace the General Partner. However, unlike the agreement in SW Acquisition, L.P., which granted the limited partners the right to replace the general partner for any "failure to achieve the business plan," the Partnership Agreement will provide a more restricted basis for replacement of the General Partner, shield the General Partner from failures that are not caused by "controllable" decisions, and, because "material failure" is defined with reference to a two-year average, permit the General Partner a reasonable period of time to correct Partnership underperformance relative to the business plan. Excluding cases of the General Partner becoming a market participant or its violation of law, gross negligence or willful misconduct, the Limited Partners will not have the right to replace the General Partner unless the General Partner makes a "controllable management decision" that results in a failure to achieve

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<sup>52</sup> As was stated in Berkshire Hathaway, Inc., the Limited Partners are aware that if they were to exert a material influence over the General Partner, the Partnership or Transco through the use of the consent rights or through a threat or suggestion involving the failure to use such consent rights, that action could constitute an "understanding" between the parties and, depending on the nature of the understanding, could result in the parties being outside the scope of this no-action letter request.

the cumulative level of earnings before interest, taxes, depreciation and amortization ("EBITDA") contemplated in the business plan by 4.5% or more, during the initial several years. A "controllable management decision" is defined as, in substance, a volitional action by management and excludes, for example, changes in law, actions of regulators, changes in demand for transmission services and other factors beyond the control of management. Furthermore, as stated in SW Acquisition, L.P., the decision to replace the General Partner would not give the Limited Partner any right to control the management of the Partnership or Transco because any replacement general partner would need to retain control over management of the Partnership and remain independent of the Limited Partner to protect the Limited Partner's status as neither a holding company nor an affiliate of a holding company or public utility company under the Act.

Finally, the terms and structure of the Transaction help to protect against any abuses under the Act and thus the Commission would have no basis to conclude that regulation of the Limited Partners under the Act is necessary or appropriate in the public interest or for the protection of investors or consumers.<sup>53</sup> After the Transaction is consummated, the General Partner, the Partnership and Transco will be privately held, and the only outside investors in the Partnership (other than the Limited Partner) will be the debt-holders, *i.e.*, certain banks that are not otherwise affiliated with the Partnership and which are in the business of lending to companies like the Partnership.<sup>54</sup> All of the investors will be sophisticated parties that will have been well informed as to the nature of their investment. Transco will remain subject to regulation by FERC under the Federal Power Act, as well as certain state regulation as to siting and safety issues by the Michigan Commission. FERC's regulation of Transco includes regulation of virtually every aspect of its transmission service through FERC's jurisdiction over Transco's open access transmission tariff and the sale of transmission services. In addition,

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<sup>53</sup> The central factors that the Commission considers in determining whether regulation is necessary or appropriate to prevent the abuses that the Act is intended to remedy are: "(1) the size of the electric utility company, (2) the nature and extent of inter-company relationships, (3) the ownership and distribution of the electric utility company's securities, and (4) the opportunity for excessive charges between the two companies for financing, service and construction contracts." Nevada Sun-Peak L.P. (citing *Detroit Edison Co. v. SEC*, 119 F.2d 730, at 739-40 (6th Cir.), cert. denied 314 U.S. 618 (1941)).

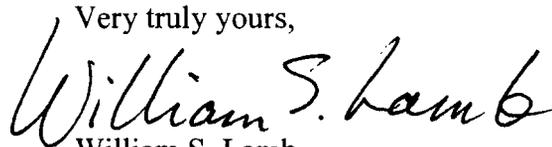
<sup>54</sup> The Partnership debt may be refinanced from time to time through banks or other lenders not affiliated with the Limited Partners.

FERC has detailed rules and regulations to protect against affiliate abuses and other potential causes of unjust, unreasonable or discriminatory rates to transmission customers. With respect to rates, as a result of a compromise with the Michigan Commission, Transco is committed to freeze its transmission rates through December 31, 2005, after which FERC retains jurisdiction over any rate changes. FERC also has approved the transfer of operational control over Transco's jurisdictional transmission facilities to MISO, which is an independent, FERC-approved RTO with operational control of the transmission assets of various electric utility companies. That transfer complies with FERC's explicit goal of promoting the independent ownership of transmission facilities.<sup>55</sup>

### III. Conclusion

For the foregoing reasons, we respectfully request that the Staff provide written confirmation that, as a result of the Transaction, it will not recommend that the Commission institute enforcement action under the Act to deem the Limited Partners to be a "holding companies" or an "affiliates" (as such terms are defined in Sections 2(a)(7) and 2(a)(11)(A) of the Act, respectively) of the Partnership, Transco or any of their subsidiaries. We would appreciate your response at your earliest convenience.

If you have any questions, please call William Lamb at (212) 424-8170 or Markian Melnyk at (202) 986-8212. If for any reason you do not concur with any of the opinions expressed in this letter, we would appreciate the opportunity to confer with you prior to any written response. Thank you.

Very truly yours,  
  
William S. Lamb

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<sup>55</sup> The instant situation is nearly identical to the facts presented in Nevada Sun-Peak L.P., in which the utility's debt and equity were held by private investors, the utility had no retail customers and its wholesale rates were fixed for a number of years under a FERC-approved contract.

# OWNERSHIP STRUCTURE

